

1 D. EDWARD HAYS, #162507
ehays@marshackhays.com
2 **MARSHACK HAYS LLP**
5410 Trabuco Road, Suite 130
3 Irvine, CA 92620
Telephone: (949) 333-7777
4 Facsimile: (949) 333-7778
5 Special Claims Counsel for Chapter 7 Trustee
RICHARD A. MARSHACK

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA, LOS ANGELES DIVISION

10 In re Case No. 2:03-bk-37579-TD
11 FOUR STAR FINANCIAL SERVICES, Chapter 7
LLC,
12 Debtor.
13
14 CHAPTER 7 TRUSTEE'S AMENDED MOTION
FOR AN ORDER MODIFYING CLAIM
OBJECTION PROCEDURES; MEMORANDUM
OF POINTS AND AUTHORITIES;
DECLARATION OF D. EDWARD HAYS IN
SUPPORT THEREOF
15
16 Date: November 4, 2009
17 Time: 10:00 a.m.
18 Ctrm: 1352
Roybal Federal Building
255 E. Temple Street
Los Angeles, CA 90012

20 TO THE HONORABLE THOMAS B. DONOVAN, UNITED STATES BANKRUPTCY
21 JUDGE, THE OFFICE OF THE UNITED STATES TRUSTEE, AND ALL OTHER
22 INTERESTED PARTIES:

23 The Chapter 7 Trustee, Richard A. Marshack (“Trustee”), of the bankruptcy estate
24 (“Estate”) of the Debtor, Four Star Financial Services, LLC (“Debtor”), files this amended
25 motion requesting entry of an Order modifying the procedure for claims objections to be filed in
26 this case (the “Amended Motion”). Specifically, the Trustee requests that the Court dispense
27 with the requirement of attaching a copy of the subject proof of claim to the multiple omnibus
28 claim objection motions filed with the Court. Trustee will provide a copy of the subject proof of

1 claim to the claimant and if any written opposition is received to an objection, the Trustee will
2 attach a copy of the subject proof of claim to his reply.

3 1. **SUMMARY OF MOTION**

4 The Trustee is in the process of filing approximately 15 separate omnibus motions
5 objecting to general unsecured claims (the “Objections”). The Objections relate to
6 approximately 400 separate proofs of claim. Unless otherwise permitted by the Court, Local
7 Bankruptcy Rule 3007(c)(2) requires that full and complete copies of all disputed proofs of
8 claim, including attachments or exhibits, be attached to any claims objection.

9 Previously, the Trustee filed an emergency motion requesting that he be excused
10 from attaching copies of each proof of claim to the Objections. In response to the filing of the
11 emergency motion, the Trustee’s staff was advised by chambers that the Court declined to set a
12 hearing on the emergency motion. By way of this Amended Motion, the Trustee renews his
13 request since it is unclear whether the Court ruled on the substance of the emergency motion or
14 whether the decision not to set a hearing was based on the lack of exigent circumstances.

15 In this case, there are approximately 451 general unsecured claims filed by
16 creditors of the Debtor. A copy of each claim already is on file with the Court. Approximately
17 400 of these claims have been filed by investors defrauded in the Debtor’s Ponzi scheme
18 (“Investors” or “Investor Claims”). Most of the Investors have filed proofs of claim for their full
19 amount of their principal plus interest at the illegal rate promised by the Debtor.

20 Pursuant to Ninth Circuit case law (and prior rulings by this Court), the Investors
21 are not entitled to include the promised illegal returns on their proofs of claim. Instead, the
22 Investors’ claims must be limited to the amount of their unpaid principal. The Trustee is in the
23 process of drafting hundreds of objections to Investor claims that have improperly included the
24 illegally promised returns.

25 To conserve the Court’s and the Estate’s limited resources, and to reduce the size
26 of the omnibus Objections, the Trustee respectfully requests that the Court dispense with the
27 requirement that a full and complete copy of each disputed proof of claim be attached to the
28 Objections filed with the Court. The Trustee will provide a copy of each disputed proof of claim

1 to the claimant and if any opposition to the Objections is filed, the Trustee will attach a copy of
2 the subject claim to his reply.

3 2. BACKGROUND

4 Prior to bankruptcy, the Debtor purported to be in the business of investing in
5 various enterprises including factoring accounts receivable for businesses with “1-900”
6 telephone numbers, internet pornography and telephone arbitrage contracts. The Debtor’s three
7 managing members were Ronald Anson, Jack Garrett and Mark Cohn.

8 Contrary to representations made to investors, the Debtor was operating a Ponzi
9 scheme. Investor losses ultimately exceeded \$60 million.

10 3. PROCEDURAL HISTORY

11 On October 24, 2003, an involuntary petition under Chapter 11 of Title 11 of the
12 United States Code was filed against Four Star Financial Services, LLC (“Debtor”). On
13 November 26, 2003, an Order for Relief was entered. On the same date, the Court entered an
14 Order directing appointment of a Chapter 11 Trustee. Richard A. Marshack was appointed the
15 Chapter 11 Trustee.

16 On March 17, 2004, an Order was entered converting this case to a case under
17 Chapter 7. On March 23, 2004, the conversion became effective. After the conversion, Richard
18 A. Marshack continued to serve as the Chapter 7 Trustee of the Debtor’s Estate.

19 The Trustee has concluded his claims review and has filed objections to priority
20 claims and secured claims. The Trustee currently is preparing objections to general unsecured
21 creditor claims.

22 Of the proofs of claim filed with the Court, many fall into the category of general
23 unsecured creditors whom “invested” money in what has been determined to be a Ponzi Scheme
24 (the “Investors”).

25 In most instances, the Investors have filed claims for the full amount of their
26 unpaid principal plus interest calculated at the illegal rate promised by the Debtor. There are
27 approximately 400 such Investors.

28 ///

1 4. LEGAL ARUGUMENT REGARDING OMNIBUS CLAIM OBJECTIONS

2 Most of Investors are seeking an allowed claim for the amount of their investment
3 plus the interest promised by the Debtor. The Investors apparently are basing their claim on a
4 'benefit of the bargain' theory which might normally govern contract claims under California
5 law. Ponzi schemes, however, are illegal and Courts will not enforce an illegal bargain. *R. M.*
6 *Sherman Co. v. W. R. Thomason, Inc.* (1987) 191 Cal.App.3d 599,236 Cal.Rptr. 577.

7 In bankruptcy cases, courts must apply principles of equity and disallow illegally
8 promised returns. *Vanston Bondholders Protective Committee v. Green*, 329 U.S. 156, 162, 67
9 S.Ct. 237, 91 L.Ed. 162 (1946) [equitable principles in bankruptcy override state law]; *Bank of*
10 *Marin v. England*, 385 U.S. 99, 103, 87 S.Ct. 274, 277, 17 L.Ed.2d 197 (1966)[“there is an
11 overriding consideration that equitable principles govern the exercise of bankruptcy
12 jurisdiction”].

13 Recovery of both false profits and the original investment would not be equitable
14 because such “profits” are paid at the expense of the later, equally innocent, investors. *In re*
15 *Tedlock Cattle Co., Inc.* 552 F.2d 1351, 1352 (9th Cir. 1977); *In re Taubman*, 160 B.R. 964
16 (S.D. Ohio 1993).

17 Based on the foregoing, the Trustee is in the process of drafting objections to
18 these approximate 400 investor claims. In previous rulings in this case, the Court has sustained
19 similar objections filed by the Trustee.

20 5. LEGAL ARGUMENT REGARDING MODIFICATION OF CLAIMS OBJECTION
21 PROCEDURE

22 Local Bankruptcy Rule 1001-1 provides that the Local Rules are to be construed
23 in a manner that promotes the just, speedy, and economic determination of every case and
24 proceeding. LBR1001-1(b)(1). The Court thus may waive the application of any Local Rule in
25 any case or proceeding, or make additional orders as it deems appropriate, in the interest of
26 justice. LBR 1001-1(d).

27 The Trustee’s accountants have calculated the amount invested, the amount
28 received and the amount of claim that each Investor should be allowed in accordance with the

1 law cited above. In the Objections, the Trustee will provide a chart for each claim which sets
2 forth the amount of the claim asserted by the Investor, the principal amount received, the amount
3 paid to the Investor and the net amount due in accordance with the law cited above.

4 The Trustee anticipates objecting to approximately 400 claims filed by Investors.
5 If each proof of claim is saved into its own computer file in Adobe Acrobat (PDF) format, the
6 size of such file would range between 50kb to more than 1 megabyte. The Court's Manual
7 requires that each electronically filed document be 2 megabytes or less.

8 The Trustee anticipates each omnibus Objection will address 10 to 15 individual
9 claims. Therefore, it is very likely that each omnibus Objection would contain at least ten
10 separate attachments. The time and effort to save these Objections and electronically file them
11 with the Court would constitute an undue expense to the Estate. Moreover, the drain on the
12 Court's Electronic Case Filing ("ECF") system would be substantial.

13 Local Bankruptcy Rule 3007-1(c)(2) provides that a copy of each proof of claim
14 subject to an objection be attached to the motion seeking disallowance. The procedures posted
15 on the Court's website for Judge Donovan likewise require copies of the disputed claims to be
16 attached to the objections. The Trustee believes that attaching approximately 400 separate
17 proofs of claim to the omnibus Objection would be a waste of Estate and judicial resources. A
18 copy of each proof of claim already is on file with the Court and the Trustee will attach a copy of
19 any disputed claim to each claimant's service copy and any reply in the event that opposition is
20 received.

21 The Trustee believes that there is good cause for the claims procedure to be
22 modified as set forth above. To strictly comply with the rule would be expensive, time
23 consuming and waste the Court's and Estate's resources. The Trustee does not anticipate any
24 opposition to the claim objections given the clear law in the Ninth Circuit.

25 The purpose of the Local Rule is to make a copy of the claim easily accessible to
26 the court when ruling on an objection. The Trustee proposes to fulfill this objective by including
27 a copy of a proof of claim in any Reply if an opposition to the objection is filed.

28 ///

DECLARATION OF D. EDWARD HAYS

I, D. EDWARD HAYS, declare as follows:

4 1. I am a partner in the firm of Marshack Hays LLP which firm is Special
5 Claims Counsel for the Chapter 7 Trustee of the above-entitled estate. If called upon as witness,
6 I could and would competently testify to the following of my own personal knowledge,
7 information and belief.

8 2. I make this Declaration in support of the Trustee's Amended Motion
9 requesting an Order Modifying the Procedure for filing objections to claims (the "Amended
10 Motion").

11 3. The Trustee's claims analysis in this case reveals that approximately 400
12 investors ("Investors") filed proofs of claim seeking an allowed claim for the amount of their
13 investment plus the interest promised by the Debtor that had been operating a Ponzi scheme (the
14 "Claims").

15 4. The Trustee believes that binding Ninth Circuit law holds that a claimant
16 defrauded by a Ponzi scheme is entitled to a claim equal to the amount of their unpaid principal.
17 Because a Ponzi scheme was an illegal enterprise, the promised profits are unenforceable.

18 5. Based on the foregoing, the Trustee is in the process of preparing
19 objections to these approximate 400 claims.

20 6. Based on provisions of the Local Bankruptcy Rules, a Trustee is required
21 to attach a copy of a disputed claim to the moving papers filed with the Court.

22 7. Based on rulings by this Court in this case, the Trustee does not believe
23 that any of the 400 Investors will file opposition to the objections.

24 8. As such, the Trustee seeks an Order permitting him to file the objections
25 without attaching copies of the disputed claims to the motion filed with the Court. However, a
26 copy of each subject proof of claim will be provided to the claimant and the Trustee will
27 summarize the amounts set forth on such claims in the motions.

1 9. If an Investor files opposition to the objections, the Trustee will attach a
2 copy of such claim to his reply. As such, the intended purpose of the Local Rules to provide the
3 Court a copy of a disputed claim in reviewing the pleadings filed in support of, and in opposition
4 to, a claims objection will be satisfied.

5 10. The task of electronically filing copies of over 400 claims as attachments
6 to the objection to claim will be unduly burdensome and time consuming to both the Trustee and
7 the Court's ECF system.

8 11. Good cause thus exists to grant this Motion as it will conserve limited
9 estate and judicial resources.

10 12. The Trustee previously requested this same relief in an emergency motion
11 filed in August 2009. In response to the emergency motion, the Court contacted my office staff
12 and advised that no hearing would be set by the Court. After learning of the denial, I asked my
13 staff to call chambers back to determine the basis of the denial (i.e. on the merits or for lack of
14 exigent circumstances). My assistant was only told that the emergency motion had been denied.
15 Given the potential savings to the Estate if the requested relief is granted, this Amended Motion
16 is filed on regular notice to determine if the previous denial was substantive or procedural.
17 Additionally, in the previous motion, Trustee did not clearly state that a copy of each subject
18 proof of claim would be provided to the claimant. With the exception of this change, the Trustee
19 concedes that no new facts or other evidence exist to bring this motion seeking reconsideration if
20 the previous denial was substantive.

21 I declare under penalty of perjury under the laws of the State of California that the
22 foregoing is true and correct.

23 | Executed on this 6th day of October 2009 at Irvine, California.

24 /s/ D. Edward Hays
25 D. EDWARD HAYS

NOTE: When using this form to indicate service of a proposed order, DO NOT list any person or entity in Category I. Proposed orders do not generate an NEF because only orders that have been entered are placed on the CM/ECF docket.

PROOF OF SERVICE OF DOCUMENT

I am over the age of 18 and not a party to this bankruptcy case or adversary proceeding. My business address is:
5410 TRABUCO ROAD, SUITE 130
IRVINE, CA 92620

The foregoing document described as **CHAPTER 7 TRUSTEE'S AMENDED MOTION FOR AN ORDER MODIFYING CLAIM OBJECTION PROCEDURES; MEMORANDUM OF POINTS AND AUTHORITIES; DECLARATION OF D. EDWARD HAYS IN SUPPORT THEREOF** was served (a) on the judge in chambers in the form and manner required by LBR 5005-2(d); and (b) in the manner indicated below:

I. TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING ("NEF") – Pursuant to controlling General Order(s) and Local Bankruptcy Rule(s) ("LBR"), the foregoing document will be served by the court via NEF and hyperlink to the document. On September 28, 2009 I checked the CM/ECF docket for this bankruptcy case or adversary proceeding and determined that the following person(s) are on the Electronic Mail Notice List to receive NEF transmission at the email address(es) indicated below:

Service information continued on attached page

II. SERVED BY U.S. MAIL OR OVERNIGHT MAIL (indicate method for each person or entity served):

On October 6, 2009 I served the following person(s) and/or entity(ies) at the last known address(es) in this bankruptcy case or adversary proceeding by placing a true and correct copy thereof in a sealed envelope in the United States Mail, first class, postage prepaid, and/or with an overnight mail service addressed as follows. *Listing the judge here constitutes a declaration that mailing to the judge will be completed no later than 24 hours after the document is filed.*

The Honorable Thomas B. Donovan - via U.S. Mail U.S. Bankruptcy Court 255 E. Temple Street, Suite 1352 Los Angeles, CA 90012	
---	--

Service information continued on attached page

III. SERVED BY PERSONAL DELIVERY, FACSIMILE TRANSMISSION OR EMAIL (indicate method for each person or entity served): Pursuant to F.R.Civ.P. 5 and/or controlling LBR, on _____, 2009, I served the following person(s) and/or entity(ies) by personal delivery, or (for those who consented in writing to such service method), by facsimile transmission and/or email as follows. *Listing the judge here constitutes a declaration that personal delivery on the judge will be completed no later than 24 hours after the document is filed.*

Service information continued on attached page

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

October 6, 2009 Layla Bergini
Date Type Name

/s/ Layla Bergini
Signature

This form is mandatory. It has been approved for use by the United States Bankruptcy Court for the Central District of California. January 2009

F 9013-3.1